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THE DELAY RENTAL AND RELATED CLAUSES OF OIL AND GAS LEASES*

HOWARD R. WILLIAMS**

The typical modern oil and gas lease provides for a relatively short primary term of five or ten years and contains a "thereafter" clause by virtue of which theoretically the interest of the lessee may have a potentially perpetual duration. Under this habendum or granting clause the lessee's interest may last forever, but it will terminate on failure of production at or after the expiration of the primary term. The interest of the lessee generally is labeled an interest in fee simple determinable, that is, a fee subject to a special limitation. Categorizing the interest has caused some difficulty in certain states where the lessee's interest may be denominated a term of years during the primary term. But if the lease survives the primary term, then clearly his interest has a potentially indefinite duration (a fee), but is subject to termination upon the happening of some event (in this case, the cessation of production) ; the lessee has, in other words, a fee on a special limitation.

THE HABENDUM CLAUSE

It is not the purpose of this paper to discuss the habendum clause of the lease in any great detail, but by reason of the interrelation of this clause with the delay rental clause, it is appropriate and necessary to mention briefly certain of the doctrines which have developed with reference to this clause of the lease.

1. With virtual unanimity the courts have declared that the lessee's interest ends automatically with the expiration of the primary term unless the event or one of the events specifically mentioned in the "thereafter" clause has occurred, and it terminates

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**Professor of Law, Columbia University.

thereafter on subsequent failure of production.¹ Neither notice by the lessor to the lessee of the termination nor re-entry by the lessor is necessary.² The termination, being automatic, cannot be waived by a lessor who seeks to recover damages for alleged subsequent breach of the lessee's obligations under the lease.³ If the lessee continues in possession of the land after the automatic termination of the lease, his possession may be categorized as that of a tenant from month to month, at sufferance, or at will.⁴ Since his original entry upon the land was by right, he does not become a trespasser, or at least not a "bad faith" trespasser, by holding over until he is directed and refuses to surrender possession.⁵

2. The termination of the lessee's original interest in the land is by virtue of the normal expiration of the granted term and is not categorized as a forfeiture. Hence the rules which have developed about the maxim, "Equity abhors forfeitures," are, in the main, inapplicable.⁶

3. The event occasioning termination of the lessee's interest is normally failure of production at or after the expiration of the pri-

1. *McDaniel v. Hager-Stevenson Oil Co.*, 75 Mont. 356, 243 Pac. 582 (1926).

2. *Taylor v. Kimbell*, 219 La. 731, 54 So. 2d 1 (1951).

3. *Joyce v. Wyant*, 105 F. Supp. 979 (W.D. Mich. 1952), *aff'd*, 202 F. 2d 863 (6th Cir. 1953).

4. *Renner v. Huntington-Hawthorne Oil & Gas Co.*, 39 Cal. 2d 93, 244 P. 2d 895 (1952) (the lessee continued in possession after the end of the primary term while production was not in paying quantities and the lessor continued to accept payment of royalties; held, the lessee became a tenant from month to month, and notice to quit was necessary to terminate the tenancy); *Moon v. Marker*, 26 Cal. App. 2d 33, 78 P. 2d 460 (3d Dist. 1938) (lessee became a tenant at sufferance when he continued in possession after end of primary term during which he had failed to produce, and hence he was not entitled to notice to surrender possession as a prerequisite to the maintenance of a suit for possession, nor was it necessary that all lessors join in the action to recover possession).

5. In *Greer v. Stanolind Oil & Gas Co.*, 200 F. 2d 920 (10th Cir. 1952), it is suggested that if the lessee holding over after the end of his term is a trespasser, he is a good-faith rather than a bad-faith trespasser, and hence he would be able to recover the value of improvements made in good faith, and, had he obtained production, he could have set off the reasonable cost of production against the recovery by the landowner of the value of the oil produced. *But cf. Humble Oil & Ref. Co. v. Kishi*, 276 S. W. 190 (Tex. Comm. App. 1925), *rehearing granted*, 291 S. W. 538 (Tex. Comm. App. 1927) in which a holdover lessee was held to be a trespasser and liable for loss in the speculative value of the premises when he drilled a dry hole.

6. See, e.g., *Watson v. Rochmill*, 137 Tex. 565, 155 S. W. 2d 783, 137 A. L. R. 1032 (1941). *But cf. Eggleston v. McCasland*, 98 F. Supp. 693 (E.D. Okla. 1951) (productive gas well drilled but lack of pipe line connection prevented marketing. After seven years during which the lessee expended substantial sums in developing the nearby area in the hope of getting a pipe line connection, the lessor claimed the lease had terminated at the end of the primary term. Held for the lessee. One of the bases for the decision of the court was its conclusion that termination of the lease under the proven facts would be inequitable.)

mary term.⁷ In construing the word "production" in this context, most courts have declared that in the light of the purposes of an oil and gas lease, production means "production in paying quantities."⁸ In other words, there must be sufficient production to permit the lessee to realize a profit over and above his costs.⁹

Since accounting is an art as well as a science, it may frequently be difficult to ascertain whether the small production which the lessee has from the premises is profitable production. Of particular importance in this connection is the determination of the share of the lessee's overhead to be attributed to the particular leasehold. There are a number of other important questions in this context. Must the lessee produce at a profit after paying both the lessor's royalty and the overriding royalty or oil payment retained by the lessee's assignor in transferring the leasehold? Apparently the latter is excluded in making this decision.¹⁰ What is the appropriate time period for ascertaining whether production is profitable? Is this to be ascertained over a period of a week, a month, or six months? Are unusual non-recurrent expenses to be included in the cost totals in making this calculation? Generally it is said that the production must be at a profit "under normal conditions" and over a reasonably long period of time.¹¹ Another question arises as to whether the lease may be kept alive if one well is producing at a profit, or if gas is being produced at a profit, even though the leasehold as a whole

7. *Town of Tome Land Grant, Inc. v. Ringle Development Co.*, 56 N. M. 101, 240 P. 2d 850 (1952) (no production from premises at end of term and questionable that gas well which had been shut in was capable of production in paying quantities; held, the lease expired at the end of the primary term).

8. See *Garcia v. King*, 139 Tex. 578, 164 S. W. 2d 509 (1942); and cases discussed by Williams, *Primary Term and Delay Rental Provisions*, Southwestern Legal Foundation, Second Annual Institute on Oil and Gas Law and Taxation 106-114 (1951). *But cf.* *Hudson v. Lyons*, 199 Okla. 348, 186 P. 2d 309 (1947). When owners of separate, non-contiguous tracts joined in a single joint or community lease, production on one of the tracts was sufficient to keep the lease alive after the expiration of the primary term on all of the tracts, even though royalties were not apportioned among all the lessors. *A. Veeder Co. v. Pan American Production Co.*, 205 La. 599, 17 So. 2d 891 (1944). See *Summers, Oil and Gas* § 298 (perm. ed. 1938).

9. The term paying quantities has a different meaning when used in the contexts of the development clause of a lease or of the implied covenants. In these contexts, a well is not producing in paying quantities unless production is sufficient to repay the cost of drilling the well. See *Renner v. Huntington-Hawthorne Oil & Gas Co.*, 39 Cal. 2d 93, 98-99, 244 P. 2d 895, 899 (1952).

10. See, e.g., *Transport Oil Co. v. Exeter Oil Co.*, 84 Cal. App. 2d 616, 191 P. 2d 129 (2d Dist. 1948) and *Vance v. Hurley*, 215 La. 805, 41 So. 2d 724 (1949), declaring that such overriding royalties or oil payments should not be included in computing costs for the purpose of determining whether production is in paying quantities.

11. *Garcia v. King*, 139 Tex. 578, 164 S. W. 2d 509 (1942); *Transport Oil Co. v. Exeter Oil Co.*, 84 Cal. App. 2d 616, 191 P. 2d 129 (2d Dist. 1948).

is producing at a loss.¹² When production is not in paying quantities, the acceptance of royalties by the lessor does not prevent him from claiming that the lease has expired by its terms.¹³

4. Drilling operations¹⁴ or production under a pooling or unitization agreement on the pool or unit but off the leased premises serves to keep the lease alive as to the portion of the premises which was included in the pool or unit¹⁵ and, under some authority, even as to the portion not included in the pool or unit,¹⁶ both during and after the expiration of the primary term. Absent statutory authority for compulsory pooling or unitization¹⁷ or authorization by the lessor to the lessee either in the lease or in a separate agreement to pool or unitize,¹⁸ production on the pooled or unitized tract but off the leased premises does not have this effect.

The harshness of the rule providing for *automatic* termination of the lessee's estate upon the occurrence of the limiting event, failure of production in paying quantities, has been ameliorated to some extent by the courts and by careful drafting of leases.

1. It is generally held that mere temporary cessation of production at or after the expiration of the primary term does not occasion termination of the lease. Obviously difficult questions may arise as to what is "temporary."¹⁹ In one case cessation of production from

12. See discussion in Williams, *supra* note 8, at 109-112.

13. Gas Ridge, Inc. v. Suburban Agricultural Properties, Inc., 150 F. 2d 363, *rehearing denied*, 150 F. 2d 1020 (5th Cir. 1945), *cert. denied*, 326 U. S. 796 (1946), *rehearing denied*, 327 U. S. 815, 327 U. S. 817 (1946); Renner v. Huntington-Hawthorne Oil & Gas Co., 36 Cal. 2d 93, 244 P. 2d 895 (1952); Loeffler v. King, 228 S. W. 2d 201 (Tex. Civ. App. 1950), *rev'd on other grounds*, 149 Tex. 626, 236 S. W. 2d 772 (1951). But such acceptance has been said to be evidence that the lease has not terminated. Vance v. Hurley, 215 La. 805, 41 So. 2d 724 (1949); Eggleston v. McCasland, 98 F. Supp. 693 (E.D. Okla. 1951).

14. McClain v. Harper, 206 Okla. 437, 244 P. 2d 301 (1952) (the lease contained a drilling operations clause; shortly before the expiration of the primary term the lessee began drilling on the unit but off the plaintiff's tract which was part of the unit).

15. Crichton v. Lee, 209 La. 561, 25 So. 2d 229 (1946).

16. Hunter Co. v. Shell Oil Co., 211 La. 893, 31 So. 2d 10 (1947); LeBlanc v. Danciger Oil & Ref. Co., 218 La. 463, 49 So. 2d 855 (1950); Gray v. Cameron, 218 Ark. 142, 234 S. W. 2d 769 (1950). The lease itself, if it authorizes pooling or unitization, or the unitization agreement, frequently expressly so provides. Jackson v. Hunt Oil Co., 208 La. 156, 23 So. 2d 31 (1945).

17. The units involved in the Hunter and LeBlanc cases, *supra* note 16, were created by the conservation commission under statutory authority. The leases were saved from termination by production on the pooled or unitized tract, both as to the portions of the leased premises included within and the portions not included within the pool or unit.

18. As in Scott v. Pure Oil Co., 194 F. 2d 393 (5th Cir. 1952), 31 Texas L. Rev. 75.

19. In Stimson v. Tarrant, 132 F. 2d 363 (9th Cir. 1942), *cert. denied*, 319 U. S. 751 (1943), suspension of production for 14 months by reason of

1930 to 1934 was held to be temporary.²⁰ It would seem that this case represents a holding contrary to the weight of authority as to the relevance of the acceptance of royalties by the lessor and other equitable considerations to the expiration of a lease under a clause of limitation. Apparently the court was reluctant boldly to announce a holding contrary to the weight of authority and hence couched its opinion in terms of "temporary" cessation of production.

2. When the failure to obtain production prior to the end of the primary term is due to wrongful acts of the lessor or to his interference with the drilling operations of the lessee, the failure of production at that time is excused if production is obtained within a reasonable time after the expiration of the primary term.²¹

3. Some cases have saved leases despite the failure to produce if a well capable of production was drilled during the life of the lease and only lack of a market postponed the beginning of production in paying quantities.²² The usual construction of the habendum clause in Kansas precludes this result, but in a recent case it was held that the presence of a drilling operations clause in the lease caused a change in the normally applicable rule.²³ The reasoning of the court was that the parties to the drilling operations clause necessarily contemplated some time lag between the completion of a well and the beginning of production, during which time the lease was kept alive after the expiration of the primary term. It then declared that consistency required that the habendum clause receive the same construction. Hence, the lease was not terminated at the end of the primary term even though there was then no production if a well had been completed during the primary term and production began within a reasonable time of its completion and of the end of the primary term. *Quaere*: is it rational to adopt a varying construction of the habendum clause based on the largely chance factor of the presence or absence of a drilling operations clause? Is the court evidencing a reluctance to apply "the normal rule of construction" in this context by grasping at a straw as the basis for the making of an exception to the "normal" rule?

absence of a market and storage facilities was found to be temporary. In *Reynolds v. McNeill*, 218 Ark. 453, 236 S. W. 2d 723 (1951), the lessee obtained production during the primary term but at the end of the term he was not producing, apparently because fine sand had filtered into the bottom of the drill casing and had obstructed the flow of oil. The court sustained the holding of the chancellor that the lessee might have sixty days of grace in which to resume paying production.

20. *Saulsberry v. Siegel*, 252 S. W. 2d 834 (Ark. 1952).

21. *Eastern Oil Co. v. Coulehan*, 65 W. Va. 531, 64 S. E. 836 (1909).

22. *Christianson v. Champlin Ref. Co.*, 169 F. 2d 207 (10th Cir. 1948).

23. *Tate v. Stanolind Oil & Gas Co.*, 172 Kan. 351, 240 P. 2d 465 (1952).

4. In a number of modern leases, the "thereafter" clause has been modified to provide that the lease may be kept alive after the expiration of the primary term by something other than production, *e.g.*, by continuous drilling operations with not more than a 60 or 90 day interval between the cessation of drilling operations on one well and the commencement of operations on another well.²⁴ An example is the following clause:

"Subject to the further provisions hereof, this lease shall continue in full force and effect for a period of five (5) years from this date, hereinafter referred to as the primary term, and as long thereafter as either (1) oil, gas, or any other mineral is produced from the land herein leased or from any land with which said land or any part thereof is then unitized as herein-after provided, or (2) the shut in well money is paid in accordance with paragraph 3(b) hereof, or (3) drilling operations are conducted in good faith on the land herein leased or on any land with which the land herein leased or any part thereof is then unitized as herein provided. As used in this lease, drilling operations shall include any activity on the leased premises or on land with which the leased premises or any part thereof is then unitized in a good faith effort to obtain, increase, improve or re-establish production from such leased premises or unit; drilling operations shall be considered as being conducted in good faith if not more than ninety (90) days are permitted to elapse between the cessation of production or drilling operations as herein defined on one well and the commencement of drilling operations on another well or hole upon the leased premises or on lands with which the leased premises or any part thereof is then unitized."²⁵

A common type of drilling operations clause (called a "well completion clause") serves to keep the lease alive after the expiration of the primary term by virtue of current drilling operations, but if the well then being drilled proves to be a dry hole, the lease may not be preserved by further operations.²⁶

Typically the courts have been liberal in finding commencement of drilling operations under clauses of these types where only the most preliminary steps have been taken towards drilling.²⁷ In such cases, however, the drilling operations must be prosecuted with rea-

24. See, *e.g.*, *Humphrys v. Skelly Oil Co.*, 83 F. 2d 989 (5th Cir. 1936); *Christianson v. Champlin Ref. Co.*, 169 F. 2d 207 (10th Cir. 1948); *St. Louis Royalty Co. v. Continental Oil Co.*, 193 F. 2d 778 (5th Cir. 1952); *Rogers v. Osborn*, 250 S. W. 2d 296 (Tex. Civ. App. 1952).

25. This clause was used in the lease construed in *West v. Continental Oil Co.*, 194 F. 2d 869 (5th Cir. 1952).

26. *Wickham v. Skelly Oil Co.*, 106 F. Supp. 61 (E.D. Okla. 1952), *aff'd*, 202 F. 2d 442 (10th Cir. 1953).

27. *Aldrich v. Gypsy Oil Co.*, 132 Okla. 13, 268 Pac. 1109 (1928); *Guleke v. Humble Oil & Ref. Co.*, 126 S. W. 2d 38 (Tex. Civ. App. 1939).

sonable diligence.²⁸ There is some doubt whether drilling operations can be said to have commenced if a well permit has not been obtained from the appropriate regulatory agency.²⁹

The shut-in gas well clause considered *infra*, may permit of the continuance of a leasehold interest despite non-production if a producing formation has been tapped and the failure to produce is due to the absence of a market. The production requirement of the "thereafter" clause has occasionally been rewritten to define the production required to keep the lease alive in terms other than "paying quantities," or to define "paying quantities" in terms of production of a given amount of oil.³⁰

THE DRILLING OR DELAY RENTAL CLAUSE

Lessors are obviously concerned with obtaining the economic benefits of an oil and gas lease at as early a date as possible. Some early leases were for long terms and contained no drilling obligations on the part of the lessees. Lessors were dissatisfied if the lessee did not commence drilling operations with reasonable diligence as no returns from the leasehold accrued to the lessor during the period of the lessee's inactivity.

One solution to this problem was the exaction from the lessee, as part of the lease, of a covenant to commence drilling operations within a relatively brief period of time and to continue drilling operations with reasonable diligence thereafter until a given number of wells had been drilled. So called "drill or forfeit" clauses of this general type are in use today in some states. They generally provide that on failure of the lessee to drill within a stated period of time, the lessor may declare a forfeiture of the lease. Typically the lessor may assert forfeiture only on the expiration of a stated time after notice of the breach to the lessee.³¹ Lessees generally are not willing

28. *Flanigan v. Stern*, 204 Ky. 814, 265 S. W. 324 (1924).

29. In *Goble v. Goff*, 327 Mich. 549, 42 N. W. 2d 845 (1950), an evenly divided court sustained a trial court decree that drilling had not been commenced despite preparatory operations on the premises by the lessee on the ground that he had not obtained the required permit to drill. Failure to obtain a well permit was viewed as indicating absence of good faith in "commencing" drilling operations in *Illinois Mid-Continent Co. v. West*, 122 Ind. App. 17, 102 N. E. 2d 390 (1951).

30. *Renner v. Huntington-Hawthorne Oil & Gas Co.*, 39 Cal. 2d 93, 244 P. 2d 895 (1952); *McLean v. Kishi*, 173 S. W. 502 (Tex. Civ. App. 1915).

31. See, e.g., *Swigert v. Stafford*, 85 Cal. App. 2d 469, 193 P. 2d 106 (2d Dist. 1948); *Prairie Oil Co. v. Carleton*, 91 Cal. App. 2d 555, 205 P. 2d 81 (4th Dist. 1949). In *Brightwell v. Norris*, 242 S. W. 2d 201 (Tex. Civ. App. 1951), on breach of a covenant by the lessee to drill, the lessor was said to be entitled in equity to a cancellation or rescission of the lease. In another part of the opinion the court declared that the lease terminated automatically on the expiration of the period allowed for drilling under the lessee's covenant.

to make such covenants except in the case of leases obtained in proven territory, and the problem of enforcing such covenants made them unsatisfactory even to the lessor with sufficient bargaining power to obtain such a covenant.

Equity rarely if ever will order specific performance of a covenant to drill,³² and the lessor will be remitted to his action for damages at law in the event of breach by the lessee. Although in some states the lessor may recover what it would have cost the lessee to perform his obligation to drill,³³ the normal rule of damages is that an injured party is entitled to be compensated for his loss. Clearly his loss is not measured by what performance would have cost the lessee but is measured by the revenues which he would have received had the lessee performed, that is, the royalties the lessor would have received had the well been drilled.³⁴

Performance of his covenant by the lessee would normally have profited the lessor in one other way.³⁵ While drilling operations were being pursued, the value of his retained royalty interest would have increased since drilling operations seem always to have this effect. Perhaps damages might be measured by the amount he could have received for the purchase of his royalty interest or by the amount which he might have obtained as a bonus for a lease on his retained land not subject to the particular lease executed to the defaulting lessee. But, entirely apart from the difficult problem of proof of what the increment would have been had drilling operations been prosecuted by the lessee, the lessor would not have suffered this loss unless he would have sold his royalty interest or executed a new lease on his retained adjacent lands. To recover damages measured

32. See Summers, *Oil & Gas* § 533 (perm. ed. 1938).

33. See, e.g., *R. Olsen Oil Co. v. Fidler*, 199 F. 2d 868 (10th Cir. 1952); *Smith v. Kious*, 194 Okla. 17, 147 P. 2d 442 (1944); *Fite v. Miller*, 196 La. 876, 200 So. 285 (1940); Note, 122 A. L. R. 446 (1939). *Contra*: *Riddle v. Lanier*, 136 Tex. 130, 145 S. W. 2d 1094 (1941) (cost of drilling well as measure of damages for breach of covenant to drill declared to have been entirely repudiated "except perhaps in cases where the cost has been paid in advance for the drilling of a well, which, when and if completed, will belong entirely to the owner of the land or leases, and in which the driller will have no interest." *Id.* at 134, 145 S. W. 2d at 1096).

34. *Guardian Trust Co. v. Brothers*, 59 S. W. 2d 343 (Tex. Civ. App. 1933) (error ref'd); *Taubert v. Earle*, 133 S. W. 2d 145 (Tex. Civ. App. 1939). It will usually be virtually impossible to prove this loss for had there been sufficient evidence to justify a jury in finding that the well if drilled or completed would have been a producer, the lessee would almost certainly have drilled the well.

35. When a covenant to drill is made in a contract other than a lease, as, e.g., when a transfer of land is made for consideration of a promise to drill, the covenantee, on breach of the covenantor, may be able to recover the value to him of the geological information which he would have obtained on the drilling of the well. *Hoffer Oil Corp. v. Carpenter*, 34 F. 2d 589 (10th Cir. 1929), *cert. denied*, 280 U. S. 608 (1930).

in this fashion, the lessor must generally prove that he would have sold and that he could have sold;³⁶ the proof of the loss of a specific opportunity to sell may be required before he will be permitted to recover damages measured in this fashion.³⁷ Because of the difficulty of proof of damages a liquidated damages clause is occasionally used.³⁸

Another solution of the lessor's problem of obtaining either early drilling operations or a periodic return from the lease was the execution of a lease with an extremely short primary term of three months to a year. Reluctance of lessees to take such leases renders this theoretical possibility of little value.

The addition of a delay rental clause to the typical oil and gas lease was the result of the search for a method assuring the lessor of some return from the leasehold during the continuance of the leasehold pending commencement of production by the lessee.

There are two types of delay rental clauses in use, the so-called "or" clause and the "unless" clause. Typical language of an "or" clause is as follows:

"Second party (lessee) agrees to commence operations on said premises within [one year] from this date, or thereafter to pay to the first party (lessor) [one] dollar per acre per annum annually until a well is drilled, or the property hereby granted is conveyed to the first party."

The "unless" clause, on the other hand, reads in general as follows:

"If operations for drilling are not commenced on said land on or before [one] year from this date the lease shall then terminate as to both parties, unless on or before such anniversary date Lessee shall pay or tender to Lessor or to the credit of Lessor in _____ Bank at _____, (which bank and its successors are Lessor's agent and shall continue as the depository for all rentals payable hereunder regardless of changes of ownership of said land or the rentals either by conveyance or by the death or incapacity of Lessor) the sum of _____ Dollars, (\$_____), (herein called rental), which shall cover the privilege of deferring commencement of operations for drilling for a period of twelve (12) months. In like manner and upon like payments or tenders annually the com-

36. *Riddle v. Lanier*, 136 Tex. 130, 145 S. W. 2d 1094 (1941).

37. *Fite v. Miller*, 192 La. 229, 187 So. 650, 122 A. L. R. 446 (1939). (The lessee assigned $\frac{1}{2}$ interest in a leasehold on consideration of a covenant to drill a well. The assignee breached the covenant. Held, proof that lessee could have sold the lease for \$5000. does not justify recovery of that sum as damages for breach of contract absent an allegation that the lessee would have sold if he had not previously assigned a $\frac{1}{2}$ interest to the assignee.)

38. *United States v. Hole*, 38 F. Supp. 600 (D. Mont. 1941).

mencement of operations for drilling may be further deferred for successive periods of twelve (12) months each during the primary term."

The distinguishing characteristic of the two types of clauses is that in the "or" clause the lessee covenants to drill or to pay delay rentals. The addition of a clause in the usual "or" lease, which permits the lessee to surrender the lease at his option upon the payment of the nominal sum of \$1 merely provides a third option for the lessee. With this clause added, he promises "to drill *or* to pay rentals *or* to surrender the lease." If he fails to surrender the lease or to drill prior to an anniversary date of the lease, the lessor may sue for and collect the rentals.³⁹

Lessees were not entirely satisfied with the "or" clause, even with the addition of a surrender clause, for generally they did not desire to make any promises concerning initial drilling operations on the land. As a result, the "unless" clause came into common use. The lessee using this clause makes no promises whatsoever as regards initial drilling.⁴⁰ He can keep the lease alive during the primary term by drilling operations or by the payment of rentals, but he is not required to do either. If he fails to do either, then the lease automatically terminates upon the anniversary date.

In short, under the "or" clause, the lessee covenants to "drill or pay," or to "drill or pay or surrender." If he does none of these things, the lessor may sue for rentals or he may forfeit the lease.⁴¹ Under the "unless" clause, the lessee covenants nothing, but the lease will terminate automatically "unless" the lessor commences drilling operations or pays rentals.

The option of the lessor to forfeit the lessee's interest for failure to commence drilling operations or pay rentals is generally construed to be akin to the common law right of entry, or, to use the phrase used in the Restatement of Property, a power of termina-

39. *Cohn v. Clark*, 48 Okla. 500, 150 Pac. 467, L. R. A. 1916B 686 (1915).

40. There usually are, of course, express or implied covenants concerning protection of the premises from drainage or development of the premises.

41. Occasionally forfeiture for failure to drill or pay has been allowed even though the lease contained no forfeiture clause. *Hickernell v. Gregory*, 224 S. W. 691 (Tex. Civ. App. 1920). Generally, however, forfeiture is not an available remedy absent an express forfeiture clause in the lease. *Girolami v. Peoples Nat. Gas Co.*, 365 Pa. 455, 76 A. 2d 375 (1950). The lessor may elect to waive his rights under a forfeiture clause and sue for rentals. *Cohn v. Clark*, 48 Okla. 500, 150 Pac. 467, L. R. A. 1916B 686 (1915) W. Va. Code Ann. § 3573 (1949) provides for forfeitures of a lease if delay rentals are not paid within 60 days after notice of default is given to the lessee and demand made for payment.

tion.⁴² As was true at common law, the termination of an estate by exercise of a right of entry or power of termination requires affirmative re-entry by the lessor, or, if the lessee resists, judicial process to obtain possession of the land. The courts treat the power of termination as a forfeiture provision. Although judicial antipathy to forfeiture clauses is not as pronounced in the case of oil and gas leases as in the case of other conveyances, courts occasionally give relief from the forfeiture when certain equities favoring the person whose interest is sought to be forfeited are found. Thus, if failure to commence drilling operations or to pay rentals was due to unforeseen and fortuitous circumstances, equity will normally grant relief from forfeiture to a lessee who is ready, willing and able to perform his obligations.⁴³

The "or" lease has substantially been replaced by the "unless" lease. Inasmuch as the lessee using this lease has covenanted nothing concerning initial drilling operations and is not liable for failure to drill, the courts have not been as anxious to protect him from forfeiture of his interest. The "unless" clause has been construed generally, therefore, as one of special limitation which operates automatically to extinguish the estate granted upon the happening of the designated event (non-payment of rentals where drilling operations have not been commenced.)⁴⁴ Historically termination of an estate by a special limitation was not treated as a forfeiture, and the equitable doctrines applicable to relief from forfeiture have been treated as irrelevant. Generally speaking the categorization of the "unless" clause as one of limitation rather than forfeiture has led the courts to say that the estate granted terminates automatically and that the equitable considerations which are relevant to the operation of the forfeiture clause of an "or" lease are irrelevant in the case of an "unless" lease. Thus, whatever the difficulties or impediments encountered by the lessee in commencing drilling operations or whatever his innocent mistake in failure to make timely and full payment of delay rentals, the lease terminates upon his failure to do one or the other by the anniversary date of the lease.⁴⁵

Under an "unless" lease, great care must be exercised in the

42. Restatement, Property § 24 (1936).

43. See Walker, Cases on Oil & Gas 522 and cases cited (1949).

44. Termination is automatic even though the lease contains a provision for notice of default to be given the lessee upon his breach of any term in the agreement. *Richfield Oil Corp. v. Bloomfield*, 103 Cal. App. 2d 589, 229 P. 2d 838 (2d Dist. 1951).

45. *Phillips Pet. Co. v. Curtis*, 182 F. 2d 122 (10th Cir. 1950).

payment of delay rentals. Thus in one case,⁴⁶ a leasehold was lost despite timely deposits of delay rentals in the depository bank when the lessee instructed the bank to credit the deposit to the lessor and his wife. Even though the land involved was community property, and therefore the wife had an interest therein, the lease had been executed by the husband alone and called for deposit of the rentals to the lessor's credit.

Sometimes the lessee is in doubt as to the person entitled to receive delay rentals. For example, he may not be sure as to the interests of two or more persons who have joined in the lease. In such a case there is authority permitting him to deposit the rentals in a bank payable jointly to all the lessors.⁴⁷ Or, if the lessee is in doubt, he may apply to a court of equity to appoint a trustee to receive the delay rentals and tender payment to the court or to the trustee prior to the due date.⁴⁸ By statute in Mississippi, it is provided that in certain situations payment may be made directly to a minor or to a parent of the minor where the minor has no guardian.⁴⁹

To guard against the possibility of dereliction in payment of delay rentals to assignees of the lessor, the lease should make specific provision to the effect that the lessee is not bound by assignments of the lessor's interest until a given number of days (*e.g.*, 30 days) after receipt of a certified copy of a recorded instrument evidencing such transfer or change in ownership.⁵⁰

Occasional trouble develops over the due date of delay rental payments. The anniversary date of the lease may be in doubt by reason of the fact that the lease is dated as of one day, executed by the lessors on another day, and perhaps acknowledged and recorded on still other days. Considerable care must be exercised in such instances. In one case,⁵¹ and "unless" lease was dated October 8, 1943 but was not delivered until November 26, 1943. Delay rentals were tendered in a subsequent year after October 8 but before November 26. The court held that the former of the two dates was the anni-

46. *Clingman v. Devonian Oil Co.*, 188 La. 310, 177 So. 59 (1937).

47. *Perkins v. Magnolia Petroleum Co.*, 148 S. W. 2d 266 (Tex. Civ. App. 1941).

48. *Stady v. The Texas Co.*, 150 Kan. 420, 94 P. 2d 322 (1939) (The lessee having failed to obtain the appointment of a trustee to receive rentals and having failed to make payment, the lease terminated. Failure to pay was not excused by the fact that the lessee did not know who was entitled to payment).

49. Miss. Laws 1944, c. 308; Miss. Code Ann. § 448 (1942).

50. The lessee may refuse to give effect to any notice not in accordance with that specified in this clause. *Pearce v. Southern Nat. Gas Co.*, 220 La. 1094, 58 So. 2d 396 (1952).

51. *Hughes v. Franklin*, 201 Miss. 215, 29 So. 2d 79 (1947).

versary date upon which rentals were due. In another case,⁵² a correction lease was executed to rectify a mistake in the first lease. The court held that the first and not the correction lease determined the anniversary date for delay rental payments. Another recent case⁵³ concerned a lease which bore the date May 20, 1947, but which was actually signed and acknowledged by the several lessors between June 12 and July 15, 1947. It was delivered on July 15, 1947. The anniversary date for payment of rentals was held to be the date the lease bore, May 20, and not the date of delivery, July 15. Difficulty in this regard can easily be avoided by specifying in the delay rental clause the date upon which payments are due.

Despite the requirement of timeliness of payment of delay rentals, there is authority that a lessee may pay rentals on Monday if the anniversary date falls on the preceding Sunday, and still keep the lease alive.⁵⁴ It is, however, usually a mistake in policy on the part of the lessee to delay payment of rentals until the last possible day; the risks involved of failure to make tender on the proper day are obviously too great.

There are some real or apparent exceptions found in a few cases to this historical approach that the "unless" clause is one of limitation which operates automatically. Among these are the following:

1. Equitable considerations may be important in that the court will be moved thereby to adopt a construction of the lease which does not involve termination of the lessee's estate.⁵⁵ Thus in a recent case,⁵⁶ production under a lease fell to approximately six barrels per day after the expiration of the primary term, an amount insufficient to pay the cost of lifting the oil, and the lease expired. The lessor and the lessee agreed to the execution of a new lease on the same premises, which was duly executed and became effective on August 5, 1947. As a result of a material advance in the price of oil in 1947, the revenue from the well increased to the extent that it exceeded the cost of operations and paid a profit. The lessee did no additional drilling and did not pay delay rentals in 1948. In an action by the lessor to establish that the new lease had terminated, the court held for the lessee. Although royalties payable to

52. *Humble Oil & Ref. Co. v. Mullican*, 144 Tex. 609, 192 S. W. 2d 770 (1946).

53. *Greer v. Stanolind Oil & Gas Co.*, 200 F. 2d 920 (10th Cir. 1952).

54. *Armstrong v. McGough*, 157 Ark. 173, 247 S. W. 790, 29 A. L. R. 236 (1923). See *Summers, Oil and Gas* § 346 (perm. ed. 1938).

55. See *St. Louis Royalty Co. v. Continental Oil Co.*, 193 F. 2d 778 (5th Cir. 1952) and cases discussed in *Williams, supra* note 8, at 117-119.

56. *West v. Continental Oil Co.*, 194 F. 2d 869 (5th Cir. 1952).

the lessor were less than the amount of delay rentals provided for by the lease, production was in paying quantities. The court construed the lease to mean that production from the well which at the time of the execution of the lease was not in paying quantities could keep the leasehold alive by virtue of the rise in price unforeseen at the time of the execution of the new lease, without the necessity of engaging in further drilling operations or the payment of delay rentals.

2. In some cases the leasehold interest has survived failure to make timely payment of rentals when an effort to make such payment was aborted by accident or mistake.⁵⁷

3. The leasehold has been permitted by other courts to continue where the lessee's failure to gain production was due to interference by the lessor with drilling operations or to his premature declaration of forfeiture or termination of the lease.⁵⁸

4. By late acceptance of delay rentals by the lessor, the lease may be saved.⁵⁹ However, if the lessor is unaware at the time he accepts payment of rentals that the lessee has failed to perform his obligations under a lease, such acceptance has been held not to bar his assertion that the lease has terminated.⁶⁰

5. Even though an inadequate payment of delay rentals is made to the owner of an undivided interest, the lease may be saved if the inadequacy of payment is due to misconstruction by the lessee of an ambiguous instrument executed subsequent to the leasing transaction.⁶¹ In a recent Oklahoma case,⁶² for example, the lessee paid the entire rental to the depository bank in ample time. Not being sure of the appropriate means of dividing the rentals among the owners of interests therein, the instruments conveying such interests being ambiguous, the lessee made no directions to the bank as to the division of the rentals. The bank credited the entire rental payment to the original lessor. The court held that the lease was

57. See *Baker v. Potter*, 223 La. 274, 65 So. 2d 598 (1953) and cases discussed in *Williams*, *supra* note 8, at 121-126, and Note, 5 A. L. R. 2d 993 (1944). Illustrative of the strict view that the lease terminates automatically on failure to make timely payment of rentals are *Vaughan v. Doss*, 219 Ark. 963, 245 S. W. 2d 826 (1952) (lessees by mistake mailed delay rentals to wrong bank); *Phillips Pet. Co. v. Curtis*, 182 F. 2d 122 (10th Cir. 1950); *Ellison v. Skelly Oil Co.*, 206 Okla. 496, 244 P. 2d 832 (1952) (delay rentals sent to wrong depository bank).

58. See cases discussed in *Williams*, *supra* note 8, at 126-127.

59. *Id.* at 127-129.

60. *Brightwell v. Norris*, 242 S. W. 2d 201 (Tex. Civ. App. 1951).

61. See *Jones v. Southern Nat. Gas Co.*, 213 La. 1051, 36 So. 2d 34 (1948) and cases discussed in *Williams*, *supra* note 8, at 129-133.

62. *Superior Oil Co. v. Jackson*, 207 Okla. 437, 250 P. 2d 23 (1952).

not terminated as to the interests of owners who had not received their proportionate share of the royalties.

It should be noted, however, that when the lessee is not required to give effect to an assignment of the lessor's interest absent a notice in specified form, if, in spite of non-receipt of the required notice, he pays rentals in accordance with his erroneous construction of an instrument executed by the lessor subsequent to the lease, he may lose all or a portion of the leasehold as a result.⁶³

6. The lease may be saved if full payment of delay rentals has been made even though such payment was made to the wrong person, the original lessor rather than his assignee, when notice of the assignment was received by the lessee subsequent to the payment of the rentals but prior to the due date of payment.⁶⁴ But, although leases typically provide that the lessee is not under a duty to pay rentals or royalties to an assignee of the lessor until he has received notice of the assignment in a specified manner, this does not excuse failure to make timely tender of rentals merely because the lessee is not sure of the person or persons entitled thereto.⁶⁵

7. Some courts have permitted revivor of a terminated lease by reference thereto in a subsequently executed instrument as a valid lease, even though such mention was not intended to revive the leasehold.⁶⁶

8. Oral modification of delay rental provisions by acceptance of substitute performance for payment of the rentals specified in the lease has been given effect to save the leasehold.⁶⁷

9. A few courts have gone so far as to suggest, at least tentatively, that equitable considerations are directly relevant to the termination of the lessor's estate under an "unless" lease, as, for example, estoppel.⁶⁸

THE NO-TERM LEASE

Occasionally, apparently nearly always by mistake or by reason of unthinking completion of blanks in store-bought forms,⁶⁹ the

63. *Atlantic Ref. Co. v. Shell Oil Co.*, 217 La. 576, 46 So. 2d 907 (1950).

64. See cases discussed in Williams, *supra* note 8, at 133-134.

65. *Stady v. The Texas Co.*, 150 Kan. 420, 94 P. 2d 322 (1939).

66. See *Loeffler v. King*, 149 Tex. 626, 236 S. W. 2d 772 (1951) and cases discussed in Williams, *supra* note 8, at 134-135. Similarly an invalid mineral deed may be made effective by recitations in a subsequent lease. *Hillmer v. Farmers Royalty Holding Co.*, 196 F. 2d 124 (5th Cir. 1952).

67. See cases cited in Williams, *supra* note 8, at 135.

68. See *St. Louis Royalty Co. v. Continental Oil Co.*, 193 F. 2d 778 (5th Cir. 1952); *Risinger v. Arkansas-Louisiana Gas Co.*, 198 La. 101, 3 So. 2d 289 (1941); *Jones v. Southern Nat. Gas Co.*, 213 La. 1051, 36 So. 2d 34 (1948), and cases discussed in Williams, *supra* note 8, at 135-137.

69. Unthinking use of forms is always dangerous. See Williams, *Hoff-*

same period of time is specified in the delay rental clause as is specified for the primary term of the lease. Thus, the blank for the duration of the primary term may be completed with the numeral "1" or the word "one" so the lease is to last for one year "and so long thereafter. . . ." Then the "unless" clause provides that the lease shall terminate one year from date if drilling operations have not then been commenced unless delay rentals are paid.⁷⁰ Construing these two clauses together, it is clear that there is in effect no primary term for the lease after which the lease can be kept alive only by production. Instead, the lease may be kept alive indefinitely by payment of delay rentals annually. The result is to create what is known as a "no-term" lease.⁷¹

Many early leases were consciously written as "no-term" leases. It is unlikely that a modern lease is intended to be for "no-term." Most "no-term" leases found to have been created by conveyances in the last two decades probably resulted from mistake or misunderstanding in the completion of the blanks in a lease form.⁷²

The "no-term" lease is sometimes construed to create an estate at will, terminable by either party,⁷³ and sometimes construed as an estate terminable by the lessor but only after notice of intent given to the lessee followed by a reasonable period of time for the commencement of drilling operations.⁷⁴ In Michigan it has been held that the primary term of one year was not extended by commencement of drilling operations despite the presence of a delay rental clause.⁷⁵ Whatever the construction of this instrument, the parties probably did not intend such consequences. The mistake is one carefully to be guarded against.

So much by way of the general characteristics of the delay rental clause and its relation to the primary term clause. Let us turn now to some of the problems which arise from the interrelation of the delay rental clause and other clauses in the lease.

man v. Magnolia Petroleum Co.: The "Subject-to" Clause in Mineral and Royalty Deeds, 30 Texas L. Rev. 395 (1952).

70. See, e.g., *J. J. Fagan & Co. v. Burns*, 247 Mich. 674, 226 N. W. 653, 67 A. L. R. 522 (1929).

71. See, e.g., *Rosson v. Bennett*, 294 S. W. 660 (Tex. Civ. App. 1927).

72. For a discussion of the no-term lease, see Summers, *Oil and Gas* § 289 (perm. ed. 1938).

73. *Lanham v. Jones*, 84 Colo. 129, 268 Pac. 521 (1928).

74. *Indiana Nat. Gas & Oil Co. v. Beales*, 166 Ind. 684, 76 N. E. 520 (1906). *Lloyd's Estate v. Mullen Tractor & Equipment Co.*, 192 Miss. 62, 4 So. 2d 282 (1941), seems to go further in suggesting that the lessee may delay drilling indefinitely by payment of delay rentals.

75. *J. J. Fagan & Co. v. Burns*, 247 Mich. 674, 226 N. W. 653, 67 A. L. R. 522 (1929). *Contra*: *Consolidated Gas Co. v. Rieckhoff*, 116 Mont. 1, 151 P. 2d 588 (1944).

THE SHUT-IN GAS WELL CLAUSE

The marketing of the product after production has been obtained sometimes causes difficulties. Where oil is produced, it is possible to transport the product to market by truck or rail, if necessary, prior to obtaining a pipe line connection. Where gas only is produced, however, truck or rail transportation does not provide a substitute for a pipe line connection to market. Until the latter is obtained, the product cannot be marketed except occasionally in relatively small quantities in the immediate neighborhood. Particularly when production is obtained only a short time before the normal expiration of the primary term of the lease, the non-availability of a pipe line connection may raise critical problems.

The shut-in gas well clause has been added to lease forms to take care of this contingency.⁷⁶ In effect, it is a definition by the parties of the word "production" in the "thereafter" clause. By virtue of inclusion of this clause, the lease will be considered to be producing in such quantities as are sufficient to keep it alive if (1) the well is capable of producing gas in commercial quantities,⁷⁷ and (2) the payment of the shut-in gas well royalty is timely and in the appropriate amount.⁷⁸ Incidentally, the sums paid under such a clause are "royalties" and not "rentals."⁷⁹

As to the latter requirement, timely payment of the full amount of the shut-in gas well royalty, we encounter the same problems which were mentioned with reference to the payment of delay rentals. The requirements as to timeliness of the payment and as to payment in full are the same. If the payment be tendered a day late or in an amount deficient by a few cents, the lease will not be kept

76. See Comment, *Clauses in Oil and Gas Leases Providing for the Payment of an Annual Sum as Royalty on a Nonproducing Gas Well*, 24 Texas L. Rev. 478 (1946); Hardwicke, *Problems Arising Out of Royalty Clauses in Oil and Gas Leases in Texas*, 29 Texas L. Rev. 790, 797 (1951); Moses, *Problems in Connection with Shut-in Gas Royalty Provisions in Oil and Gas Leases*, 23 Tulane L. Rev. 374 (1949), 27 Tulane L. Rev. 478 (1953). Early clauses of this type applied only to wells from which "gas only" is produced. The clause has been rewritten to apply to wells from which "gas and/or distillate only" is produced. Variants in this clause are numerous. The word "only" has been omitted from some shut-in gas well clauses, and many leases expressly define a gas well to include wells capable of producing natural gas, condensate, distillate or any gaseous substance, and wells classified as gas wells by any government authority.

77. *United States v. Brown*, 15 F. 2d 565 (N.D. Okla. 1926); *Taylor v. Kimbell*, 219 La. 731, 54 So. 2d 1 (1951).

78. *Freeman v. Magnolia Pet. Co.*, 141 Tex. 274, 171 S. W. 2d 339 (1943).

79. So held in *Morriss v. First Nat. Bank*, 249 S. W. 2d 269 (Tex. Civ. App. 1952) (error ref'd n. r. e.), and hence owners of non-participating royalty interests are entitled to share in the payment. *Accord*, *Risinger v. Arkansas-Louisiana Gas Co.*, 198 La. 101, 3 So. 2d 289 (1941).

alive.⁸⁰ In one case, however, where the lease contained a clause providing that the lessee might keep the lease alive by resuming drilling operations within 90 days of the cessation of production subsequent to the end of the primary term, it was held that payment of the shut-in royalty within 90 days of shutting-in a gas well kept the lease alive.⁸¹ A difficult question as to the anniversary date for payment in subsequent years could arise from such a holding.

Since the payment is of royalty rather than rental, the rule that non-payment of royalty is not grounds for cancellation of a lease is said to be applicable. But, unless paid, the lease may fail on the anniversary date unless delay rentals are paid, and will fail at or after the expiration of the primary term by reason of lack of production.⁸²

A recent Louisiana case illustrates the interrelation of several clauses of a lease.⁸³ The lease was for 10 years and contained a "thereafter" and an "unless" clause. It also contained a shut-in gas well clause, providing that if the shut-in gas well royalty were paid, it would be considered that gas was being produced within the meaning of the primary term clause. The lease also contained a dry hole clause, requiring the resumption of drilling operations or of rentals on the drilling of a dry hole prior to discovery of oil or gas.

During the primary term the lessee drilled a well which was capable of producing gas in paying quantities but, no market then being available, the well was shut-in. Neither delay rentals nor the shut-in gas well royalty was paid. The lessors then sought an order cancelling the lease. The court denied them this relief. The reasoning of the court was as follows:

1. The payment of the shut-in gas well royalty was optional with the lessee. No forfeiture was provided for in the event of his failure to pay such sum.

80. *Freeman v. Magnolia Petroleum Co.*, 141 Tex. 274, 171 S. W. 2d 339 (1943).

81. *Shell Oil Co. v. Goodroe*, 197 S. W. 2d 395 (Tex. Civ. App. 1946) (error *ref'd*, n. r. e.).

82. " * * * upon cessation of production after termination of the primary term, the lease automatically terminates. * * * Here the parties agreed that if no gas was being produced on April 7, 1940, the lease should terminate. They further agreed that a gas well from which gas was not being sold or used off the premises was a producing well provided a royalty of fifty dollars was paid. Clearly, then, if the fifty dollars was not paid on or before April 7, 1940, gas was not being produced from the premises on that date, and the lease terminated for nonproduction. That is precisely what the contracting parties said should follow, and they were privileged to define what they meant by the phrase 'a producing well.' " *Freeman v. Magnolia Petroleum Co.*, 141 Tex. 274, 278, 171 S. W. 2d 339, 341 (1943).

83. *Sohio Petroleum Co. v. V. S. & P. R.R.*, 222 La. 383, 62 So. 2d 615 (1952).

2. The lease required drilling operations or resumption of rentals to keep the lease alive if a dry hole were drilled prior to discovery of oil or gas; but this was not a dry hole, so this clause of the lease is inapplicable.

3. The "unless" clause provided for the termination of the lease if no well was drilled, unless rentals were paid. But, a well was drilled, so the lessee was not required to pay rentals to keep his lease alive.

Thus, under this lease it was possible, by virtue of the drilling of a gas well capable of producing in paying quantities, to keep the lease alive during the entire primary term without production or the payment of delay rentals or shut-in gas well royalties. Then, just before the expiration of the primary term, the lessee might elect to pay the shut-in gas well royalty and keep the lease alive thereafter as a "producing" well. Obviously the lease should be drafted to avoid this consequence. The delay rental, shut-in gas well, and dry hole clauses should be carefully interrelated so as to insure some return to the lessor during the primary term if the lessee is not engaged in drilling operations after the drilling of the first well which is capable of producing in paying quantities but which does not so produce for lack of a market.

Many early shut-in gas well royalty clauses were poorly drafted from the viewpoint of the lessor in that they called for a payment of a relatively small amount annually which might serve to keep the leasehold alive on a substantial tract without further obligation to continue drilling operations (except insofar as such an obligation is imposed by the implied covenants of the lease) and without further payment of delay rentals. The sum required to be paid under this clause should be sufficiently substantial as to encourage the lessee to seek diligently to obtain a pipe line connection, and should be equal in amount, at least, to the delay rentals previously payable to keep the lease alive, or, in the alternative, the lease should provide that the payment of royalty under this clause should suffice to keep the lease alive only as to a given number of acres.

The requirement as to the timeliness of the payment becomes of special importance in view of the fact that the anniversary date under this clause is rarely, and then only by happenstance, the same as the anniversary date for the payment of delay rentals. Under this clause, the payments are usually due on the anniversary of the shutting-in of the gas well.⁸⁴ An example may point up the problem.

84. *Superior Oil Co. v. Stanolind Oil & Gas Co.*, 240 S. W. 2d 281 (Tex. 1951), 30 Texas L. Rev. 780 (1952), raised the related problem as

A lease was duly executed and delivered on June 1, 1950. The anniversary date upon which delay rentals was due, was, therefore, June 1. During the first year a well was drilled and gas in commercial quantities discovered. The well was shut in on May 1. To keep the lease alive after June 1, normally payments under the delay rental or shut-in gas well clause must be made on or before June 1.⁸⁵ To keep the lease alive by virtue of the shut-in gas well clause, payments are due in subsequent years on or before May 1.⁸⁶ If the payments under the delay rental and shut-in gas well clauses are identical in amount, the lease may be kept alive during the primary term by payments made prior to June 1 of each year, the lessee asserting the benefit of the delay rental clause.⁸⁷ But, to keep the lease alive after the primary term, or to keep it alive during the primary

to the anniversary date under a "dry-hole" clause. The anniversary date of the lease was March 3. The anniversary of the dry hole was February 3. For three years subsequent to the drilling of the dry hole, delay rentals were paid prior to February 3 "for the period of February 3, 194.... to February 3, 194...." The Lessee assigned the leases to defendants in December, 1948, and defendants tendered rentals to the lessors on February 5, 1949, which tender was refused because payment had not been made by February 3. The court could not agree on the construction of the lease involved in this case but held, two judges dissenting, that the anniversary date for the payment of rentals was changed to the date of the completion of the dry hole by the contemporaneous construction of the parties to an ambiguous instrument, and hence the leasehold terminated on February 3, 1949 for failure to pay rentals. The problem as to the due date of payments is the same under a dry-hole and under a shut-in gas well clause.

It seems generally understood that the shut-in gas well royalty is due annually in advance, in the absence of specific provision in the lease to the contrary, and is due initially when the well is shut in. See Walker, *supra* note 76 at 480. Many leases provide that the anniversary date of the lease is the due date for payments under the shut-in royalty. Hardwicke, *supra* note 76, at 799.

85. Under the "unless" clause, the drilling of a well during the year may excuse payment of rentals at the next ensuing anniversary date. Payment usually must be resumed or new drilling operations commenced on or before the second anniversary date.

86. *Morris v. First Nat. Bank*, 249 S. W. 2d 269 (Tex. Civ. App. 1952) (error ref'd, n. r. e.), makes it clear that payment of the shut-in gas well royalty will keep a lease alive during the primary term without further payment of delay rentals or commencement of drilling operations.

87. Some doubt as to whether a lease may be kept alive during the primary term by payment of delay rentals, as opposed to payment of the shut-in gas well royalty, is raised by *Morris v. First Nat. Bank*, *supra* note 86. The royalty clause (paragraph 3 of the lease) contained a shut-in gas well provision that while the shut-in royalty was paid, such well shall be held to be a producing well under paragraph 2 of the lease (the primary term clause). The delay rental clause (paragraph 4) provided that if oil, gas or other mineral is not being produced on the anniversary date, the lease shall terminate unless delay rentals are paid. The court declared that "After production the option to pay delay rentals, provided by paragraph 4, ceased. * * * Since the fact of production did exist, the lease did not terminate upon a failure to comply with the delay rental provision of paragraph 4. But after production, paragraph 3 required the lessee to pay royalty. Hence, the royalty under paragraph 3 was required to be paid, and the rentals under paragraph 4 were not required to be paid after production." *Id.* at 273.

term by payments under the shut-in gas well clause, where that is to the lessee's interests by reason of the fact that it is a smaller sum than delay rentals, the sum is due on or before May 1, rather than on or before June 1 of each year.

Another problem as to the anniversary date may be raised by virtue of that fact that sometimes after the shutting-in of a gas well, it may be reopened for the sale of gas to lessees drilling on adjoining premises or for use by the lessee on another lease. Royalties must be paid for such production. If after a period of production for such purposes the well is again shut-in, the question arises as to whether this creates a new anniversary date for payment of the shut-in gas well royalty.

It should perhaps be emphasized that the shut-in gas well royalty clause does not modify the implied covenants to use reasonable diligence in marketing the gas⁸⁸ and to develop the premises with reasonable diligence.⁸⁹

INTER-RELATION OF THE RENTAL AND OTHER CLAUSES IN A LEASE

One construction of the delay rental clause is that it has no effect upon the habendum clause, and hence if, at the expiration of the primary term, there is no production, the leasehold terminates even though drilling operations are then being pursued which result in production the next day.⁹⁰ In some states, however, the delay rental clause is held to enlarge the habendum clause as follows. If drilling operations begin during a period for which delay rentals have been paid, the lease continues so long as such drilling operations are pursued with reasonable diligence.⁹¹ There is much to be said for the latter position, but the lessee should not leave the matter in doubt in drafting the lease. It is a relatively simple matter for him to provide specifically for the continuance of the term of the lease after the primary term if drilling operations are in effect at its expiration. When the lease contains such a clause, the courts require that the operations be pursued with reasonable diligence to avoid extinguishment of the lessee's interest.⁹² Neither a drilling clause of this type nor a shut-in gas well clause will change the lease from a

88. *Risinger v. Arkansas-Louisiana Gas Co.*, 198 La. 101, 3 So. 2d 289 (1941).

89. *Amerada Pet. Corp. v. Doering*, 93 F. 2d 540, 114 A. L. R. 1385 (5th Cir. 1937).

90. *J. J. Fagan & Co. v. Burns*, 247 Mich. 674, 226 N. W. 653, 67 A. L. R. 522 (1929).

91. *McClanahan Oil Co. v. Perkins*, 303 Mich. 448, 6 N. W. 2d 742 (1942); *Hicks v. Mid-Kansas Oil & Gas Co.*, 182 Okla. 61, 76 P. 2d 269 (1938); *Consolidated Gas Co. v. Rieckhoff*, 116 Mont. 1, 151 P. 2d 588 (1944).

92. *Flanigan v. Stern*, 204 Ky. 814, 265 S. W. 324 (1924).

determinable fee to a fee on condition subsequent. Such clauses are effective only to redefine the event or condition upon the occurrence of which the lease will terminate.

As has been noted previously, to keep a lease alive after the expiration of the primary term it is normally necessary that there be production and that the production be in paying quantities. The question arises as to whether the lease may be kept alive during the primary term without the payment of delay rentals by virtue of production which is not in paying quantities. In at least one case,⁹³ the suggestion has been made that any production will keep the lease alive during the primary term and, moreover, that discovery without further payment of delay rentals or production, may have that effect during the primary term. Obviously the lessee should, for safety's sake, resume payment of rentals during the primary term if his production is not in paying quantities.

The lessor should scrutinize with great care the delay rental clause in the lease submitted to him for signature lest it provide that the drilling of a well during the primary term will serve to keep the lease alive for the balance of the primary term without production, further drilling operations, or payment of rentals. Such was the effect of a lease provision construed in a Kentucky case.⁹⁴ The lease provided that the lessee shall drill and complete a well "on said premises within six months from the date hereof, or pay annually in advance at the rate of \$1.50 an acre per year for each additional year such completion is delayed. . . . [I]t is further agreed . . . that the completion of a well . . . shall be and operate as a full liquidation of all rental under this provision during the remainder of the term of this lease"⁹⁵

The drilling of a dry hole in the first six months under this lease was held sufficient to keep the lease alive for the balance of the primary term without the necessity of payment of delay rentals.

The lease should be specific as to the date upon which delay rentals are to be resumed during the primary term in the event a dry hole is drilled and there is no production from the premises. Otherwise, controversy and litigation is invited. Thus, in *Wilson*

93. *Cox v. Miller*, 184 S. W. 2d 323 (Tex. Civ. App. 1944) (error ref'd.) The lease contained a dry hole clause requiring resumption of drilling operations or payment of rentals to keep the lease alive. A well capable of producing gas in paying quantities was drilled but shut-in for lack of a market. The suggestion that the well was not a dry hole meant that the lease might be kept alive during the balance of the primary term without resumption of rental payments.

94. *Unity Oil Co. v. Hill*, 200 Ky. 651, 255 S. W. 151 (1923).

95. *Id.* at 652-653, 255 S. W. at 152.

v. Wakefield,⁹⁶ the Kansas Supreme Court construed a lease executed on October 10, 1935, containing a delay rental and a dry hole clause. The former was in usual form, providing that "if no well be commenced" on or before October 10, 1936, this lease shall terminate unless the sum of \$160 is paid, "which sum shall operate as a rental and cover the privilege of deferring the commencement of a well for twelve months from said date. In like manner and upon like payments or tenders the commencement of a well may be further deferred for like periods of the same number of months successively."⁹⁷ The dry hole clause provided that if the first well be a dry hole, then if a second well is not commenced on said land within twelve months from the expiration of the last rental period for which rental has been paid, the lease shall terminate unless before the expiration of said twelve months the lessor shall resume the payment of rentals.

During the first year of the lease the lessee drilled a dry hole which was completed on or about April 15, 1936. No rental was paid before October 10, 1936, and on May 12, 1937, after the expiration of twelve months from the anniversary of the dry hole, the lessors sued to cancel the lease. The court held for the lessee, declaring that the payment of rentals on the first anniversary date of the lease subsequent to drilling of the dry hole was excused. Payment of delay rentals or commencement of drilling operations on or before the next succeeding anniversary date was requisite to the continued validity of the lease.

Although payment of rentals may be suspended by drilling operations, most modern leases provide for the resumption of delay rentals during the primary term when the well or wells drilled are dry or when production ceases. The lease should be more specific as to the date on which rentals or drilling operations are to be resumed than was the lease construed in this case. The alternatives are three: (1) on the lease anniversary date next succeeding the completion of the well, (2) on the first anniversary of the completion of the dry hole, or (3) as in this case, on the second anniversary date of the lease after the completion of the dry hole. One of these alternatives should be expressly provided for by the lease with such explicitness as to avoid the possibility of controversy over the construction of the language.

The lease construed in a recent case⁹⁸ illustrates the care that

96. 146 Kan. 693, 72 P. 2d 978 (1937).

97. *Id.* at 694, 72 P. 2d at 979.

98. *Glasscock v. Sinclair Prairie Oil Co.*, 87 F. Supp. 915 (S.D. Tex. 1950), *aff'd*, 185 F. 2d 910 (5th Cir. 1950).

should be used in drafting the delay rental clause. This lease provided that:

"Operations for the drilling of a well or reworking operations on any well on said land or production from any well thereon shall continue this lease in force only in so far as this lease covers a tract for each such well with respect to which operations for drilling are being conducted, or on which reworking operations are being conducted, or from which production is being obtained, containing not more than 640 acres of land (for each such well) to be designated by Lessee, such respective tracts of not more than 640 acres to be of such shape or configuration as may be designated by Lessee with the well on any part thereof. * * * The aforementioned rental payable by Lessee to cover the privilege of deferring commencement of operations for the drilling of a well for periods of twelve (12) months each during the primary term shall be reduced by an amount equal to One Dollar (\$1) per acre for each acre of land including within any tract or tracts which Lessee is holding or entitled to hold on the due date of the rental payment in question, by virtue of the designation by Lessee prior to such due date of a tract or tracts as above provided and the conduct of drilling or reworking operations thereon or obtaining production therefrom."⁹⁹

Under this clause the lessor is insured of a return on the leasehold during the primary term. However, to the lessor's chagrin, this clause was held to be applicable only to the primary term, and the entire leasehold of 8400 acres was kept alive by production from two wells after the expiration of the primary term.

EFFECT OF ASSIGNMENTS OF THE WORKING INTEREST

Not infrequently litigation results from the division of the lessee's interest subsequent to the lease and failure by one of the owners of a portion of the working interest to begin drilling operations or to pay rentals prior to the anniversary date of the lease. If division of the leasehold is not specifically authorized by the lease, the owner of a divided interest in the leasehold may not keep the lease alive as to his interest merely by paying the proportionate share of the rentals attributable to his interest.¹⁰⁰ However, if there are drilling operations in effect on the portion of the leasehold held by another operator, he need not pay rentals at all.¹⁰¹ Similarly, if after the expiration of the primary term there is production from a portion of the leasehold held by another, this will suffice to keep the leasehold

99. *Id.* at 916.

100. See Merrill, *The Partial Assignee—Done in Oil*, 20 Texas L. Rev. 298, 301 (1942).

101. See Walker, *Cases on Oil and Gas* 813 (1949).

in its entirety.¹⁰² There may be, of course, liability on the covenants in the lease, express or implied, for development, which may result in cancellation of the lease in whole or in part.¹⁰³

If, however, the lease specifically provides for the possible division of the working interest, as is usually the case, normally it will further provide that the working interest in a segregated portion of the leased premises may be kept alive by payment of the proportionate part of the delay rentals attributable thereto.¹⁰⁴ By agreement of the parties to the division of the working interest, it may be provided that one will pay delay rentals for all, and this will apparently be given effect. If, however, the owner of the working interest in a segregated portion of the tract, absent such a prior agreement, fails to make timely payment of delay rentals, the fact that the owner of another subdivided portion pays the full delay rentals due under the lease will not serve to keep the former's interest alive.¹⁰⁵

In Louisiana, production on one part of the divided leasehold

102. *Berry v. Tidewater Associated Oil Co.*, 188 F. 2d 820 (5th Cir. 1951).

103. See *State ex rel. Shell Pet. Corp. v. Worden*, 44 N. M. 400, 103 P. 2d 124 (1940).

104. *Dorman Farms Co. v. Stewart*, 157 Ark. 194, 247 S. W. 778 (1923); *Pearce v. Southern Nat. Gas Co.*, 220 La. 1094, 58 So. 2d 396 (1952). In *Flanigan v. Stern*, 204 Ky. 814, 265 S. W. 324 (1924), the lease permitted partial assignments of the working interest and provided that defalcations of an assignee should not affect the lessee as to his retained interest provided he complied with his leasehold obligations as to his unassigned portions. The lessee purported to assign 19½ acres of his 20 acre leasehold and tendered rentals for the ½ acre retained. It was held that the lease terminated on failure to pay the rentals for the full 20 acres on the ground that the lessee "had no right to keep the lease alive on any portion of the premises, which he might select by relinquishing *without consideration* and without any *bona fide assignment*, such portions of the lease as he found himself unable to retain by the payment of the required rent. The right of assignment given to the lessee under the lease contemplated a *bona fide* assignment of described and designated portions of the lease, and there is no proof that any such was made in this case. Were the rule otherwise plaintiff in this case, and other lessees adopting a similar course, could relieve themselves of the payment of any part of the obligated rent by giving away the greater undivided part of the leased premises and retaining an insignificant portion which they deemed most valuable, and thereby reducing the amount of rent required to be paid by him in order to keep the remaining holdings alive. The law has no other name for such conduct except that of a fraudulent scheme never contemplated by the parties and never enforced by the courts." *Id.* at 819-820, 265 S. W. at 326. *Accord*, *Young v. Jones*, 222 S. W. 691 (Tex. Civ. App. 1920).

There is some authority to the effect that the provision in a lease permitting division of the working interest by implication permits the owner of the leasehold in a segregated portion of the tract to keep his interest alive by paying a ratable share of delay rentals. *Hitson v. Gilman*, 220 S. W. 140 (Tex. Civ. App. 1920). This position is said to be unacceptable in *Merrill*, *supra* note 100, at 302.

105. *White v. Hunt*, 193 Miss. 742, 10 So. 2d 539 (1942). *But cf.* *Broyles v. Gilman*, 222 S. W. 685 (Tex. Civ. App. 1920).

will not serve to keep the lease alive on another portion of the divided leasehold.¹⁰⁶ The weight of authority is contra; a producing well on one portion of the leased premises will serve to keep the entire leasehold alive both during the primary term without further payment of rentals, and after the expiration of the primary term.¹⁰⁷ The lessor's only remedy thereafter against the lessee and his assignees is on the covenants in the lease, express or implied.¹⁰⁸

If an undivided share of the working interest is transferred, as opposed to the transfer of the entire working interest in a segregated portion of the tract, it would not seem that payment of a ratable share of delay rentals would be sufficient to keep the interest alive.

In the *Southland Royalty Co.* case,¹⁰⁹ similar questions were raised as to a joint or community lease. The Supreme Court of Texas held that production on one of the leased tracts serves to keep the lease alive as to all included tracts, and commencement of a well on any one of the tracts operates to excuse the payment of delay rentals on all included tracts.

THE PROPORTIONATE REDUCTION CLAUSE

Even though the lessor is believed to own only an undivided interest in a tract of land, it is frequently the practice for an oil and gas lease to purport to convey to the lessee the entire fee. The purpose in so phrasing the lease is to give the lessee the benefit of application of the doctrine of after-acquired title and to convey to him the entire interest of the lessor if it turns out to be greater than was believed to be the case. Obviously the covenants of title should be phrased to cover only the interest believed to belong to the lessor, or he may be held liable for their breach despite the parties' knowledge that the lease purported to convey more than the lessor had.¹¹⁰

A "proportionate reduction" clause is frequently included in a lease. Typical language of such a clause provides that, "In case said lessor owns a less interest in the above described land than the entire and undivided fee simple estate therein, then the bonus, royalties and rentals herein provided for shall be paid lessor only in the

106. *Roberson v. Pioneer Gas Co.*, 173 La. 313, 137 So. 46, 82 A. L. R. 1264 (1931); *accord*, *Goble v. Goff*, 327 Mich. 549, 42 N. W. 2d 845 (1950).

107. See the discussion in *Berry v. Tidewater Associated Oil Co.*, 188 F. 2d 820 (5th Cir. 1951).

108. *Cosden Oil Co. v. Scarborough*, 55 F. 2d 634 (5th Cir. 1932); see *Walker, Cases on Oil and Gas* 813-814 (1949).

109. *Southland Royalty Co. v. Humble Oil & Ref. Co.*, 249 S. W. 2d 914 (Tex. 1952).

110. See *Klein v. Humble Oil & Ref. Co.*, 126 Tex. 450, 86 S. W. 2d 1077 (1935), 14 Texas L. Rev. 563 (1936); *Griffin v. Stanolind Oil & Gas Co.*, 133 Tex. 43, 125 S. W. 2d 545 (1939).

proportion which his interest bears to the whole and undivided fee."¹¹¹

Care should be exercised either to strike the word "rentals" from the proportionate reduction clause when the lessor owns only an undivided interest in the land or to increase proportionately the amount provided for by the lease for delay rentals, so that after proportionate reduction, the lessor will receive the rentals agreed upon for his undivided interest. Thus, if the lessor owns an undivided one-half interest for which interest a 50 cent per acre delay rental is bargained for, and if the lease purports to convey the entire fee in the tract, either rentals should be deleted from the proportionate reduction clause or the rental clause should provide for \$1 per acre rental. The former practice would seem preferable as payment of a rental smaller than is provided for by the delay rental clause may give rise to friction and litigation. This practice does, of course, deprive the lessor of the benefit of the proportionate reduction clause as to rentals in the event the lessor owns a smaller interest than was supposed.

The proportionate reduction clause should be carefully examined even if the lease purports to convey no more than the undivided interest believed to be owned by the lessor. This clause usually provides for a reduction in bonus, rentals and royalties if the lessor owns less than the entire fee simple. Does this mean that these items are to be proportionately reduced even if the lessor owns the undivided interest purported to be conveyed? In a recent Texas case this problem was raised.¹¹² The lease purported to convey only the undivided $\frac{1}{2}$ interest owned by the lessor, but the proportionate reduction clause called for a reduction in bonus, rentals and royalties if the lessor owned less than the entire fee simple "in said land." The lessor paid only one-half of the full delay rentals specified in the lease, claiming that by operation of the proportionate reduction clause the lessor was entitled only to a ratable share of the rentals. The lease was held to terminate on failure to pay the full delay rentals required by the express terms of the lease.

The court concluded that when the "lessee agreed to pay \$160 rental on said land, said land referred to the interest therein conveyed by the lessor, namely, lessor's undivided one-half interest. * * * The property referred to as the land is the same as that actually owned and conveyed by the lessors. * * * Having determined

111. *Reeves v. Republic Production Co.*, 177 S. W. 2d 1011 (Tex. Civ. App. 1944) (error ref'd, w.o.m.).

112. *Texas Co. v. Parks*, 247 S. W. 2d 179 (Tex. Civ. App. 1952).

that the lessee agreed to pay lessor \$160 annual delay rental for the interest conveyed, it necessarily follows that appellant could not rely upon the reduction clause to reduce the payment from \$160 to \$80. The appellee's title has not failed. They owned the entire fee simple in what they conveyed, to-wit, their undivided one-half interest."¹¹³

This opinion dictates careful reconsideration of the language appropriate for the proportionate reduction clause where the lease purports to convey a lessor's undivided interest in the land. The clause should be modified to provide for a reduction only if the lessor owns less than the undivided interest conveyed by the granting clause of the lease.

RELATIONSHIP OF DELAY RENTAL CLAUSE AND COVENANTS OF LESSEE

The relationship between the delay rental clause and the covenants of the lease is also important. Acceptance of rentals under a lease has been held to waive performance of the duties of the lessee under express or implied covenants despite the presence in the lease of a forfeiture clause. Thus in *Sun Oil Co. v. Oswell*,¹¹⁴ a lessor sought to obtain forfeiture of the lessee's interest for failure to develop the premises. The rule applicable to this type of case was said to be "that the acceptance of delayed rental payment precludes the lessor from forfeiting the lease for failure to develop during the term covered by the delayed rental. In such a case the lessor still has the gas and has received the reserved rent for the delay in drilling. * * * The allegations of the bill mean that on September 9, 1950, a payment was made by the lessee Sun and received by the complainants of their part of the \$200 [delay rentals] under said lease. That circumstance, as heretofore stated, was a waiver of any default which had existed up to that time, if there was any, and by express terms in the lease extended the right of the lessee for another twelve months within which to perform its duty which arose under the contract, whether expressed or implied. Within twelve months after September 9, 1950, and on the 2d day of July, 1951, this bill was filed. So that at the time the bill was filed the lessee Sun was not in such default under the terms of the contract as to justify a forfeiture thereof and that without regard to whether it had failed up to that time to comply with the same."¹¹⁵ If the lessor is to have an action for breach of the covenants of a lease during the primary

113. *Id.* at 182.

114. 258 Ala. 326, 62 So. 2d 783 (1953).

115. *Id.* at 335, 62 So. 2d at 790-791.

term, he must reject tender of delay rentals and instead give notice of the breach and demand for performance of the lessee's covenants.

The weight of authority seems to be in accord with this decision that the acceptance of delay rentals excuses performance by the lessee of his covenants, express or implied, as regards protection against drainage or engaging in drilling operations. Clearly if the lessor refuses a tender of rentals he may thereafter pursue his normally available remedies for the lessee's failure to develop the premises or to protect the premises from drainage.¹¹⁶ In some cases it is said that the lessor must advise the lessee of the drainage, inform him that no further rentals will be accepted, and make a demand for the commencement of drilling operations. No cause of action arises during the period for which delay rentals had been paid if they are paid after notice to the lessor,¹¹⁷ or unless notice of breach of the covenant was given to the lessee and demand made for performance.¹¹⁸ However, the lessee cannot successfully contend that the refusal of the tendered rental and demand for a protection well will terminate the lease and relieve him from liability for drainage.¹¹⁹

In Louisiana a distinction is drawn between express and implied covenants. Acceptance of rentals with knowledge of a breach of an implied covenant is said to operate as a waiver of any right of action either for damages or for forfeiture, but where there is an express covenant to drill an offset well, the acceptance of rentals will not constitute a waiver of the rights of the lessor under the covenant.¹²⁰

In Texas, however, it has been held that acceptance of delay rentals with knowledge of existing substantial drainage is not a

116. *Poindexter v. Lion Oil Ref. Co.*, 205 Ark. 978, 167 S. W. 2d 492 (1943) (conditional decree of cancellation ordered); *Deep Rock Oil Corp. v. Bilby*, 199 Okla. 430, 186 P. 2d 823 (1947).

117. *Orr v. Comar Oil Co.*, 46 F. 2d 59 (10th Cir. 1930) ("It is our conclusion that a lessor who accepts delay rentals, before necessity for offset drilling has arisen or without knowledge of such necessity, does not waive a breach of the implied covenant to drill off-set wells; but a lessor who accepts delay rentals, after the necessity for such off-set drilling has arisen and is known to him, waives the performance of the implied covenant to drill off-set wells during the period for which such delay rentals are accepted." *Id.* at 63); *Lindow v. Southern Carbon Co.*, 5 F. Supp. 818 (W.D. La. 1932); *Carson v. Ozark Nat. Gas Co.*, 191 Ark. 167, 83 S. W. 2d 833 (1935); *Clear Creek Oil & Gas Co. v. Brunk*, 160 Ark. 574, 255 S. W. 7 (1923); *Carter Oil Co. v. Samuels*, 181 Okla. 218, 73 P. 2d 453 (1937); *Carper v. United Fuel Gas Co.*, 78 W. Va. 433, 89 S. E. 12, L. R. A. 1917A 171 (1916).

118. *Rowe v. Ashland Oil & Ref. Co.*, 240 S. W. 2d 61 (Ky. 1951).

119. *Arkansas Nat. Gas Corp. v. Pierson*, 84 F. 2d 468 (8th Cir. 1936).

120. *Hood v. Southern Production Co.*, 206 La. 642, 19 So. 2d 336 (1944); *accord*, *Stanley v. United Fuel Gas Co.*, 78 W. Va. 793, 90 S. E. 344 (1916).

waiver of the implied covenant to drill a protection well during the period of delay in the commencement of a well covered by the rental period.¹²¹ This position has also been taken by the Supreme Court of Mississippi. In the *Millette* case¹²² the court implied a covenant by the lessee to conserve the interests of its lessors by protecting against or compensating for the lessee's own act of drainage from adjacent premises. It then held "that the acceptance of the delay rentals in May 1949 does not per se estop the appellants to claim damage by way of waste caused by provable drainage through the affirmative action of their lessee. By repetition, we emphasize that the option to defer actual drilling by the payment of annual delay rentals affects only the specific right which such rentals are designed to purchase. Acceptance of such rentals is relevant solely to the duty to drill; they are not compensation for waste or depletion. Under this form of lease, the lessor may drill wells or pay rentals, but on the other hand he must prevent drainage or pay damages."¹²³

PERORATION

The importance of care in the drafting of an oil and gas lease is obvious. Not merely is it important that care be exercised in drafting the individual clauses of the lease which have been the concern of this paper, but it is vital that the relationship *inter sese* of the several clauses of a lease be carefully analyzed. A lessor which in recent years has executed leases on very substantial tracts in a producing state decided a little more than a year ago to prohibit assignments by the lessee without the lessor's consent, and it added a new printed term to the lease form which it used, providing that "This lease shall be assignable only on written consent of the lessor." Entirely apart from the serious question of the validity of such restraint on the alienation of the fee interest of the lessee, the propriety of the employment of this clause is made even more doubtful by the fact that an earlier clause of the form, left unchanged in this revision, provides that "If the estate of either party hereto is assigned — and the privilege of assigning in whole or in part is expressly allowed — * * *"¹²⁴ This form is still being used. Surely it is timely for interested parties carefully to read and analyze the lease forms in use.

121. *Texas Co. v. Ramsower*, 7 S. W. 2d 872 (Tex. Comm. App. 1928).

122. *Millette v. Phillips Pet. Co.*, 209 Miss. 687, 48 So. 2d 344 (1950).

123. *Id.* at 706, 48 So. 2d at 348-349.

124. Inevitably this lease form is labelled "Producers 88". Are there any "unless" lease forms in use which are not so labelled?